

U.S. **Network** Corporation

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May 29, 1996

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Office of the Secretary
Federal Communications Commission
1919 M Street, N.W., Room 222
Washington, D.C. 20554

Re: FCC Docket No. 96-98

Dear Office of the Secretary:

I have enclosed an original and sixteen (16) copies of USN Communications, Inc.'s ("USN") Reply Comments ("Reply Comments") in the above captioned docket and a copy also sent along with a diskette to Janice Myles of the Common Carrier Bureau. Moreover, a copy of the Reply Comments was mailed to the Commission's copy contractor, International Transcription Services, Inc., on today's date.

If you have any questions, please contact Robert Neumann at 312-906-3592.

Sincerely,

Ronald W. Gavillet/gla

Ronald W. Gavillet
Executive Vice President
and General Counsel

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**Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554**

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In the Matter of)

Implementation of the Local Competition)
Provisions in the Telecommunications Act)
of 1996)

CC Docket No. 96-98

**REPLY COMMENTS OF
U.S. NETWORK CORPORATION**

**Ronald W. Gavillet
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Summary

U.S. Network Corporation, a pioneering company in the local services resale market, respectfully replies to issues raised in the comments of certain parties regarding the pricing of wholesale services.

As the Commission has long recognized, the resale of telecommunications services plays a critical role in the development of competition and in the realization of its benefits. Some parties in the comment round of this proceeding have suggested that the resale of local services be restrained by tying the level of the wholesale discount for retail services to the combined rate for unbundled network elements. Such a suggestion is both contrary to the straight-forward, bifurcated pricing approach developed by Congress and is insupportable.

Quite simply, Congress developed two different pricing approaches: one for the wholesale pricing of retail services and one for the pricing for unbundled network elements.

Congress adopted two, unique approaches because the products are not interchangeable; they play very different roles in the development of a competitive local market. To tie the two pricing structures together would directly contradict the expressed intent of Congress when it composed the different pricing approaches and would severely constrain the robust development of a competitive local market.

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Reply Comments

U.S. Network Corporation ("USN") hereby submits these reply comments in response to the comments filed with the Commission in the Notice of Proposed Rulemaking ("NPRM") in the above-captioned proceeding.

I. Introduction.

USN is a pioneering company in the local resale market. Its affiliates are in the business of providing bundled local and long distance resold telecommunications services to small and medium sized businesses in major metropolitan markets in the country. Its affiliate, USN Communications, recently entered into three historic, broadbased resale agreements with Ameritech for Illinois, Michigan, and Ohio and is in the process of beta testing and implementing those agreements. USN works with its suppliers of local and long distance services on a daily basis to provision and maintain its growing customer base. While USN is still a relatively small company, with just under 200 employees, it is well-capitalized and plans to be a leading provider of resold local services.

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Most importantly, for purposes of this proceeding, USN speaks from a perspective of experience. Hard-earned and real experience in reselling local services. It is from that perspective that USN offers these reply comments.

II. Resale Plays a Critical Role in the Realization of the Benefits of Competition.

As the NPRM recognized (para. 8) and as further supported in the comments, see, e.g., Comments of Competitive Telecommunications Providers at 91-94, resale plays a critical role in the realization of the benefits of competition. The long distance market, which owes much of its development to the existence of strong FCC policies favoring unrestricted resale, continues to grow today because of the positive role in the market played by resellers bundling and packaging commodity communications services creatively to meet unique needs of end users. Similarly, competition in the local market will also develop based upon policies that promote unrestricted resale.

Recognizing the important role of resale in the opening the local market, Congress specifically provided for the development of a strong resale market by both establishing the affirmative obligation on the part of incumbent local exchange carriers ("ILECs") to offer retail services for resale (Section 251 (c) (4)) and in devising a unique pricing formula for wholesale services. (Section 252 (d) (3)).

III. The Wholesale Pricing Formula Necessarily Differs From The Pricing Structure For Unbundled Network Elements Because The Services Are Different.

The wholesale pricing standard contained in Section 252 (d) (3) is based on retail rates minus avoided costs, whereas the pricing standard for unbundled network elements in

Section 252 (d) (1) is based on cost and may include a reasonable profit. As recognized in the comments of the United States Telephone Association (at page 75), because of the difference between the nature of the two offerings (bundled resale services versus unbundled network elements), “[t]he rates have different starting points and different ending points....they are simply not the same, and cannot be made the same without doing violence to the language of the statute.” The intent of Congress was to establish separate and distinct pricing standards for the wholesale services versus unbundled network elements.

Indeed, as the NPRM recognized (para. 86), the unbundled network elements allows a carrier to configure a much broader set of products offerings than the bundled resale offering: “By contrast, an entrant that merely resells a bundled retail service at wholesale rates, would not receive access revenues.” This elementary difference in product provisioning capability is the reason for difference in pricing formula. The rate for wholesale bundled services must be keyed to the incumbent carrier’s retail rate, because that is the competing local service. By reducing that rate by the ILEC’s avoided costs, Congress essentially limited resale entry to carriers that operate at least as efficiently as the incumbent carrier.

IV. The Commission Should Reject The Suggestion That It Should Constrain The Pricing Of Wholesale Services By Tying It To The Pricing Of Unbundled Network Elements.

As noted above, the Congress correctly keyed the rate for wholesale services to the retail rates of the incumbent carrier. A small number of commenting parties suggested that

wholesale rates should also be tied to the combined costs for unbundled network elements. See, e.g., ALTS at Attachment A page 29 ("The resale price of any service, whether retail, wholesale, or term-and-volume discount of any sort, may not be less than the total price of the equivalent network elements provided pursuant to section 251 (c)(3)...."). This recommendation is contrary to Congress' intent and would severely suppress the development of competition in the local market.

Tying wholesale rates to the combined costs of network elements would be expressly contrary to the decision of Congress to set two pricing standards. If Congress wanted them tied together, it would have tied them together. Or more simply, there would have been a single pricing formula in the Act for both wholesale services and unbundled elements. These distinct pricing approaches were not tied together because they should not be tied together. As noted above, the underlying services for which these standards were adopted are not the same; they are not "apples to apples" products. Unbundled elements combine to allow a provider to offer local dial tone plus potentially many more services, including local switched access. In comparison, wholesale offerings are necessarily limited to resale of the ILECs retail offerings.

Moreover, in order for resale to play an effective role in the development of competitive choice in the market, resale rates must be competitive with the retail rates that are in the market *today*. Applying an ancillary and arbitrary pricing constraint on the rates for local resale rates versus the retail rates in the market would bar resale rates from playing the role of facilitating market competition.

Congress' simple, straight forward calculation of resale rates got it right -- "retail less avoided costs" allows efficient resellers to substitute their support services for the incumbent carrier's avoided services and provide a competitive product.

V. Rate Rebalancing Is A Necessary Condition Precedent to Any Imputation Test.

The few commenting parties suggesting that wholesale rates be tied to the rates for unbundled service elements in reality appear to be seeking economically cost-based local retail rates. Assuming that is their real objective, these parties should focus on attaining that goal rather than on restraining resale entry by suggesting that it meet some form of imputation test. Arbitrarily manipulating the rates for wholesale services without addressing the rates for retail services will not resolve the issue of whether retail rates are costs based. Competitive local facility-based carriers will still have to deal with the pricing of the retail rates regardless of whether resellers are in the market.

In light of the substantial rate rebalancing that potentially is triggered by the passage of the new Act, the Commission should recognize that while the concept of imputation may be attractive from an economic sense, from a practical perspective. It will likely take several years before incumbent carriers move to the cost-based retail pricing which is assumed in applying imputation. See, e.g., Illinois Commerce Commission Docket 83-0142 -- the deloading of non-traffic sensitive access costs to end-users was transitioned over several years. In addition, assuming imputation is found to be necessary, any imputation test for unbundled network elements would have to be applied in the aggregate across the

complete basket of ILEC competing retail services made possible by the unbundled network elements (e.g., dial tone, switched access).*

CONCLUSION

USN respectfully commends the Commission for stepping up to the aggressive challenges of implementing this historic piece of legislation. In order to preserve the critical role that Congress carved into the local market for resellers, USN requests that the Commission reject the suggestion to constrain the pricing of wholesale services and move swiftly to adopt rules consistent with Congress' clear objectives promoting the resale of local services.

Respectfully submitted,

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* Most importantly, it is a dangerous assumption for parties to think that the total cost of the unbundled network elements, when added up, should yield a rate at or below a cost-based retail rate. ILECs are in the business of selling bundled, end-to-end products. Requiring unbundling does not guarantee that the unbundled elements will cost less than the whole. For example, buying the individual parts of a car from a car manufacturer costs a great deal more than buying the bundled or assembled car.